

DEPARTMENT OF STATE REVENUE

Revenue Ruling #99-01 ST

March 16, 1999

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superceded or deleted by publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

Sales/Use Tax – Sale and Installation of Floor Coverings

Authority: Rule 45 IAC 2.2-3-7, Rule 45 IAC 2.2-3-9

The taxpayer requests the Department to rule on the application of sales/use tax to the sale and installation of floor coverings. To that end the taxpayer submitted the following questions.

1. Whether or not the sale and installation of each of the floor coverings sold and installed by the taxpayer is a sale of tangible personal property or an improvement to real estate?
2. Whether or not the first time installations of the floor coverings by the taxpayer are treated differently than the repair or replacement of same when installed in existing construction?
3. Whether or not the installation of floor coverings by the taxpayer in residential structures is treated differently than floor coverings installed in nonresidential structures?
4. Whether or not the form of contract used (i.e., lump sum, cost plus, time and materials with upset/guaranteed price, or separated fee) for the installation of floor coverings by the taxpayer impacts the classification as tangible personal property or an improvement to real estate?

STATEMENT OF FACTS

The taxpayer has several locations in Indiana which sell and install floor coverings in Indiana. The floor coverings include, but are not limited to, carpet, carpet tile, linoleum, sheet vinyl, vinyl tile, ceramic tile, terrazzo, marble, hardwood floors, and cove base.

Each location operates independently from other locations and maintains an autonomous controller and/or operations manager as well as distinct financial statements. In some cases, locations may even compete with one another. A location engages in either retail/residential floor covering services ("Retailers") or commercial floor covering services ("Contractors").

Retailer Operations

Retailers sell floor coverings within the state primarily to residential customers. Retailers maintain sales facilities in the state. Although customers may arrange for installation themselves, Retailers usually provide installation services. Retailers install floor coverings primarily through independent contractors and occasionally through employees. In all cases, Retailers are contractually obligated to perform installation services. The contracts for installed floor coverings may be either lump-sum or separated-fee contracts.

Retailers maintain inventories of pads, limited subflooring supplies, and minor amounts of carpet and noncarpet floor coverings. Most materials are ordered on a per job basis. These inventories may be maintained either on site or by a local distribution facility.

Contractor Operations

The taxpayer has Contractors in bordering states that primarily act as general contractors for installation services in commercial structures and sometimes as subcontractors for contracts solicited by general contractors. Occasionally, contracts for installation in residential structures are accepted, but generally, are for new residential communities. Upon contract acceptance, Contractors provide and install the floor coverings.

Contractors may, on occasion, sell floor covering materials over the counter. These types of isolated, occasional, or casual sales are generally accommodations to large commercial customers or sold as remnants or miscellaneous "material only" sales. These sales generally consist of less than 5% of total revenue.

Contractors generally do not maintain sales facilities. They may maintain a small amount of inventory, but they primarily order materials on a per job basis. The contracts for installation services may be either on a lump-sum basis or a separated-fee basis.

Installation Processes

Wall-to-wall carpet can be installed by two methods, tack strips or glue. Under the tack strip method, the installer staples or glues a carpet pad to the subfloor. The carpet is then attached over the pad to a tack strip which is nailed to the edges of the subfloor. Under the glue method, the carpet is glued directly to the subfloor. Removing tacked down carpet usually tears the carpet and damages the subfloor. To remove glued carpet, the customer must cut the carpet and rip it up. The carpet is not reusable, and the surface floor may need repair before a new floor is installed.

Carpet tile can be installed by two methods, glue or release adhesive. Under the glue method, the tile is glued directly to the subfloor. It may be removed after installation but is generally only removed and replaced when damaged or worn. Thus, glued down carpet tile is not normally reusable. Further, the subfloor may need repair due to residual glue. Under the release adhesive method, carpet tile is attached to the floor by an adhesive which allows for easier removal and/or movement. As a practice, carpet tiles are not moved until they are damaged or worn. Again, the subfloor may need repair due to residual adhesive.

To install sheet vinyl and vinyl tile floors, the installer creates a smooth subsurface over the subfloor and underlayment. The installer then glues vinyl to the underlayment. Vinyl is usually removed with a hammer and chisel or like instruments. Sometimes heat is used to soften the glue. Removing sheet vinyl destroys the flooring and damages the subfloor.

Ceramic tile generally requires the installer to trowel a thin bead of mortar on the floor and then set a durock board into the mortar. The durock board is also secured by nails. The ceramic tile is then glued to the durock board. To remove the ceramic tile, a jackhammer or crowbar is required to break up the ceramic tiles and durock layer, thus destroying the tile and damaging the subfloor. Ceramic tile can also be installed on a recessed floor by setting the tiles in a bed of concrete. Using this method, there is no way to remove the tile without destroying the tile and subfloor.

Terrazzo is installed in a mud process similar to that employed in laying concrete. The installer pours, smooths, and hardens the material onto the subfloor. There are no tiles laid. Removal destroys the terrazzo and subfloor.

Marble is installed by precasting the marble in blocks and setting it in mortar. The installation process is similar to installing bricks. Removing the marble floor would destroy the marble and the subfloor.

Hardwood floors are generally installed over an existing underlayment. The underlayment is attached through the board with ring-shanked nails. The installer trowels out glue and sets the wood floor. Boards are then nailed together on the subfloor. The hardwood floor could be removed with a hammer and chisel or like instruments. The

removal would generally damage the hardwood floor, destroy the underlayment, and damage the subfloor.

Cove base is a transition piece of rubber material used to finish or cover the edges of walls. Removing cove base requires stretching and bending it out of shape. Cove base is not reusable after removal.

QUESTION #1 – DISCUSSION

"Construction Material", pursuant to Rule 45 IAC 2.2-3-7, means any tangible personal property that is used for incorporation in or improvement of a facility or structure constituting or becoming part of the land on which such facility or structure is situated. A "contractor" converts construction material (tangible personal property) into realty and includes general or prime contractors, subcontractors and specialty contractors. It can be seen then, initially all property is defined as tangible personal property and it is the ultimate use of the tangible personal property that determines whether or not the tangible personal property remains such or becomes an improvement to realty. In the instant case, the taxpayer incorporates construction material (tangible personal property) such as wall-to-wall carpet, carpet tile, sheet vinyl and vinyl tile, ceramic tile, terrazzo, marble, hardwood and cove base into a structure, therefore, is statutorily defined as a "contractor". The taxpayer, when installing permanently attached floor coverings in structures is disposing of tangible personal property that by use becomes an improvement to real estate.

QUESTION #1 – RULING

The Department rules that the taxpayer is a statutory "contractor", and by definition, when installing permanently attached floor coverings in structures (incorporated into same) is disposing of tangible personal property that by use becomes an improvement to real estate.

QUESTION #2 – DISCUSSION

The Indiana Sales/Use Tax Code and Regulations do not differentiate between tangible personal property that is converted into realty in new construction versus tangible personal property that is converted into realty in existing construction, hence, first time installations of permanently attached floor coverings are treated the same for the application of sales/use tax as the repair or replacement of permanently attached floor coverings.

QUESTION #2 – RULING

The Department rules that first time installations of permanently attached floor coverings (new construction) by the taxpayer are treated the same for the application of sales/use tax as the repair or replacement of permanently attached floor coverings by the taxpayer (existing construction).

QUESTION #3 – DISCUSSION

The Indiana Sales/Use Tax Code and Regulations do not differentiate between tangible personal property that is converted into realty in residential structures versus tangible personal property that is converted into realty in nonresidential structures, therefore, the installation of permanently attached floor coverings in residential structures is treated the same for the application of sales/use tax as the installation of permanently attached floor coverings in nonresidential structures.

QUESTION #3 – RULING

The Department rules that the installation of permanently attached floor coverings by the taxpayer in residential structures is treated the same for the application of sales/use tax as the installation of permanently attached floor coverings by the taxpayer in nonresidential structures.

QUESTION #4- DISCUSSION

Rule 45 IAC 2.2-3-9 provides that when a statutory contractor, such as the taxpayer is when installing permanently attached floor coverings in structures, bills a project on a time and material basis (or a variant of same) the contractor is required to collect sales/use tax from the customer on all construction materials transferred to the customer. When a statutory contractor bills a project on a lump sum basis (labor and materials transferred are stated as a combined charge) the contractor is required to pay sales/use tax on all construction materials transferred to the customer. The form of contract used on a project does not impact the ultimate classification of the property transferred on the project, i.e., the property remains tangible personal property or becomes an improvement to real estate determined by its use.

QUESTION #4 – RULING

The Department rules that the form of the contract used by the taxpayer on a project does not impact the ultimate classification of the property transferred on the project, i.e., the property remains tangible personal property or becomes an improvement to real estate determined by its use.

CAVEAT

This ruling is issued to the taxpayer requesting it on the assumption that the taxpayer's facts and circumstances, as stated herein, are correct. If the facts and circumstances given are not correct, or if they change, then the taxpayer requesting this ruling may not rely on it. However, other taxpayers with substantially identical factual situations may rely on this ruling for informational purposes in preparing returns and making tax

decisions. If a taxpayer relies on this ruling and the Department discovers, upon examination, that the fact situation of the taxpayer is different in any material respect from the facts and circumstances given in this ruling, then the ruling will not afford the taxpayer any protection. It should be noted that subsequent to the publication of this ruling, a change in a statute, regulation, or case law could void the ruling. If this occurs, the ruling will not afford the taxpayer any protection.

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